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No. 81-2367

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

SOLITRON DEVICES, INC., BENJAMIN FRIEDMAN, JAMES S. TRAGER and JAMES P. BARRY,

Petitioners,

—against—

HOWARD SIROTA and FAMILY RESTORATIONS, a Partnership, on behalf of themselves and all others similarly situated,

Respondents.

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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The petition herein for a writ of certiorari to the United States Court of Appeals for the Second Circuit was filed with this Court on June 25, 1982. On July 23, 1982, respondents filed a brief in opposition to the petition. Petitioners respectfully submit this reply brief in response.

I.

THE RECENT DECISION OF THIS COURT IN *GENERAL TELEPHONE COMPANY OF THE SOUTHWEST V. FALCON* MANDATES THE SUMMARY REVERSAL OF THE DECISION BELOW.

Respondents' brief in opposition makes no mention of the recent decision of this Court in *General Telephone Company of the Southwest v. Falcon*, 50 U.S.L.W. 4638 (June 14, 1982). We believe that the decision is dispositive of the main issue raised by this petition: Is a District Court precluded from conducting a factual inquiry to determine whether a named plaintiff's claim is typical of the class claim under Rule 23(a) of the Federal Rules of Civil Procedure?

In *Falcon*, this Court held that it was "error for the District Court to presume that respondent's claim was typical of other claims against petitioner" and that the failure of the District Court to "probe behind the pleadings before coming to rest on the certification question" was reversible error. 50 U.S.L.W. 4641. As noted in the petition, the District Court in this case held that it was precluded from going beyond the pleadings in determining whether respondents' claims were typical of the class claims:

> The Supreme Court has held in *Eisen v. Carlisle & Jacquelin*, 417 U.S. 150 (1974) that the court on a Rule 23 motion lacks power to "conduct a preliminary inquiry into the merits of a suit in order to determine whether it may be maintained as a class action." From the limited vantage point permitted under the *Eisen* doctrine, the series of statements and reports relied upon by plaintiffs *in their pleadings* provide the essential continuity of omissions and misrepresentations necessary to bring the period from May 5, 1967 to March 20, 1975 within the scope of the common questions requirement. (Emphasis added) (71a-72a*).

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* References are to the appendix to the petition.

In *Falcon*, this Court reversed the certification decision precisely because the lower court failed to go beyond the pleadings in assessing the qualifications of class representatives. It is, therefore, clear that the District Court, in the instant case, erred as a matter of law and that this Court should summarily reverse the decision below.

In *Falcon*, respondent claimed that he had been denied promotion because he was of Mexican-American descent and that his employer's promotion policies discriminated against Mexican-Americans as a class. His complaint asserted that his employer discriminated against all Mexican-Americans who were or might be employed by it with regard to the terms and conditions of employment. Before trial, respondent asked the lower court to certify a class consisting, not only of all Mexican-Americans employed by his employer, but also of other Mexican-Americans who had applied for employment but had not been hired.

The lower court did not hold an evidentiary hearing to determine whether respondent's claim was typical of the claims of the class he sought to represent, nor did it make findings of fact on that issue. On the contrary, the court certified the class solely on the basis of allegations in the complaint that respondent and other class members had suffered from the same discriminatory policy of the employer.

On appeal, the Fifth Circuit held that merely by *alleging* that he had suffered from employment practices which were part and parcel of the employer's policy of racial discrimination, respondent had satisfied the requirements of Rule 23(a). This Court granted certiorari and reversed.

This Court held that the complaint in *Falcon* provided an insufficient basis for concluding that the adjudication of respondent's claim of discrimination in promotion would require the decision of any common questions concerning the failure of the employer to hire more Mexican-Americans. It noted that "[w]ithout any specific presentation identifying the questions of law or fact that were common to the claims of respondent and of the members of the class he sought to represent, it was

error for the District Court to presume that respondent's claim was typical of other claims against petitioner by Mexican-American employees and applicants." 50 U.S.L.W. at 4641. This Court emphasized that the lower court had erred in failing to "evaluate carefully the legitimacy of the named plaintiff's plea that he is a proper class representative under Rule 23(a)." 50 U.S.L.W. at 4641. Indeed, this Court clearly defined the scope of the inquiry which is appropriate under Rule 23(a):

> As we noted in *Coopers & Lybrand v. Livesay*, 437 U.S. 463, "the class determination generally involves considerations that are *'enmeshed in the factual and legal issues comprising the plaintiff's cause of action.'* " *Id.*, at 469 (*quoting Mercantile Nat. Bank v. Langdeau*, 371 U.S. 555, 558). Sometimes the issues are plain enough from the pleadings to determine whether the interests of the absent parties are fairly encompassed within the named plaintiff's claim, *and sometimes it may be necessary for the court to probe behind the pleadings before coming to rest on the certification question*. (Emphasis added) (40 U.S.L.W. 4641).

In sum, in *Falcon*, this Court held that the question of maintainability of a class action under Rule 23(a), by its very nature, involves the specific factual elements of the plaintiff's claim and that a District Court cannot rely on a complaint's conclusory allegations in determining whether the requirements of Rule 23(a) have been satisfied.

In their complaint in the case at hand, respondents did not make the factual showing which *Falcon* requires. On the contrary, the relevant allegations of the complaint contained only generalizations and conclusory statements:

> *Class Action Allegations*
>
> 7. Plaintiffs bring this action on behalf of themselves and representatively on behalf of all other similarly situated purchasers (except defendants and their privies) of the securities of Solitron during the period July 7, 1967 through March 20, 1975, and who have

either sold said securities at a loss or retained them. The purchasers of the securities of Solitron within that period of time comprise a class within the meaning of Rule 23 of the Federal Rules of Civil Procedure.

8. During the aforesaid period of time, the Solitron securities were publicly traded. The number of persons purchasing Solitron common stock and debentures during the aforementioned period of time are so numerous as to make it impractical to bring them all before the Court.

9. There are common questions of law and fact involved herein which predominate over questions affecting individual members of the class.

10. The questions of law and fact include (a) whether there has been a plan and scheme and common course of conduct to issue false and inflated financial statements and information relating to defendant Solitron; (b) whether the information disseminated by the defendants to the public during the relevant period contained untrue statements of material facts and/or failed to disclose all material facts with respect to, among other things, the profitability of certain contracts with the Federal government; the value of the inventory of defendant Solitron; the retained earnings of defendant Solitron; the sales, income, expenses, and costs of goods sold of defendant Solitron; and the potential liability of defendant Solitron for the publication of inaccurate, false and misleading financial statements and reports; (c) whether as a result of the defendant's issuance and dissemination of false and misleading statements, the market price of Solitron's securities was artificially inflated and (d) whether the conduct alleged herein of defendants violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder and common law, and whether defendants are liable to plaintiffs and other members of the class.

11. The claims of the plaintiffs herein are typical of the members of the class. Plaintiffs purchased Solitron securities during the relevant period. They have no interest which is antagonistic to the interest of the class.

12. A Class Action will be superior to other available methods for the fair and efficient adjudication of the claims set forth herein. The claims of most members of the class would be too small to justify instituting costly litigation on their behalf. Unless this action is maintainable such individuals will not be able to obtain redress. When the liability of the defendants has been adjudicated, claims of all members of the class can be filed and determined by the Court.

13. The Class Action will force the orderly and expeditious administration of the class claims with economies of time, effort and expense. The action presents no difficulties which would impede its management by the Court as a class action.

The allegations of the complaint were clearly deficient. In it (¶ 11), respondents did not state when they purchased their shares of Solitron stock and just what false financial material respecting Solitron artificially inflated the market at that time. They alleged only that they had purchased "during the relevant period." When petitioners attempted to show that respondents had purchased their stock after the Press Release and that accordingly they had no claims, or at best that their claims were not typical of the class claims, the District Court held that *Eisen* precluded it from making such an inquiry.

Obviously, as reflected in this Court's decision in *Falcon*, the District Court should have held a hearing to determine whether plaintiffs' claims were typical of the class claims in light of the issuance of the Press Release. Instead, it relied on the conclusory allegations of the complaint and allowed respondents to bootstrap their way into control over the interests of a class of utter strangers. Again, in *Falcon*, this Court noted that the

"class action device was designed as 'an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only.' " 50 U.S.L.W. at 4640 (*Quoting Califano v. Yamasaki*, 442 U.S. 682, 700-701 (1979)).

Finally, *Falcon* removes any doubt as to the propriety of corrective measures if it appears that a certification was improper: "Even after a certification order is entered, the judge remains free to modify it in the light of subsequent developments in the litigation." 50 U.S.L.W. 4641. In the case at hand, the District Court observed that "if hindsight were foresight, [plaintiffs] shouldn't have been designated as class representatives because of the dates," but then went on to hold that it was powerless to remedy the error. (13a, n.1). On this, alone, there should be a reversal.

In sum, the District Court should have held a hearing to determine whether plaintiffs' claims were typical of the class claims. Moreover, when, after trial, it became apparent they were not, the District Court should have decertified the class. This Court should, therefore, issue a writ of certiorari to the Second Circuit and summarily reverse the decision below. *E.g.*, *Rogers v. Calumet National Bank*, 358 U.S. 331 (1959); *Times Film Corp. v. City of Chicago*, 355 U.S. 35 (1957); *Securities & Exchange Commission v. Otis & Co.*, 338 U.S. 843 (1949).

II.

THERE WAS NO INQUIRY AS TO THE QUALIFICATIONS OF THE WOULD-BE CLASS REPRESENTATIVES PRIOR TO TRIAL.

Although respondents' brief makes no mention of *Falcon*, it does seek, by assertions contrary to both the record and the facts, to avoid the rule expressed in *Falcon*. It suggests that in fact there was a factual inquiry into whether plaintiffs' claims were typical of those of the class, by reference to the order of the District Court of October 29, 1976 (Respondent's Brief at 2-3). In fact, the District Court did not conduct the type of inquiry contemplated by *Falcon*. The District Court made

perfectly clear in its decision of February 13, 1979, that in certifying the class it relied exclusively on the complaint:

> From the limited vantage point permitted under the *Eisen* doctrine, the series of statements and reports relied upon by plaintiffs *in their pleadings* provide the essential continuity of omissions and misrepresentations necessary to bring the period from May 5, 1967 to March 20, 1975 within the scope of the common questions requirement. (Emphasis added) (71-72a).

III.

VARIOUS MISCELLANEOUS ERRORS IN RESPONDENTS' BRIEF.

Respondents now assert that their claims were typical of the claims of the class because the Press Release of December 14, 1970 itself was fraudulent. (Respondent's Brief at 3-4, 6-7). They reason that the Press Release only reported a loss of $7,000,000, whereas the audited year-end figures reflected a loss of $10,000,000. In the first place, the Press Release reflected the results of a 9-month period, and the audited financials reflected the results of a 12-month period. Obviously, there is nothing inconsistent about a $7,000,000 loss for a 9-month period and a $10,000,000 loss for a 12-month period. Indeed, one would not have to be too astute to anticipate higher year-end losses.

Furthermore, as pointed out in our petition, no evidence whatsoever of error, let alone fraud, was introduced at trial or at any other stage of the proceedings respecting the Press Release. Thus, following trial, when they deemed themselves safely "in the saddle," respondents readily abandoned the claims of the only class which they had any right to represent.

Respondents also argue that the jury entered a verdict for the entire period, including the dates of their purchases long after the curative Press Release. (Respondents' Brief at 3-4). As the record reflects, the jury entered verdicts across-the-board based upon set percentages of the damages testified to

by respondents' expert witness. Three of the six years in question were set aside by the District Court on the grounds that there was no evidence whatsoever to support the verdict, and of the remaining three years, one was substantially reduced by the Court of Appeals. The cutoff occasioned by the Press Release was actually stipulated to by respondents at the conclusion of the trial in order that the jury not be given an interrogatory respecting the separate period following the release of the price announcement. At any rate, the District Court, as already noted, made perfectly clear its own conclusion respecting the effect of the release and the viability of any claim by the respondents.

CONCLUSION

For the foregoing reasons, a writ of certiorari should be granted.

Dated: August 2, 1982

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